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SUPREME COURT

IN THE
SUPREME COURT OF THE UNITED STATES

October Term, 1974

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No. 74-1073

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FIRST NATIONAL BANK OF OREGON,
a National Banking Association,

Petitioner,

v.

AMERICAN TIMBER & TRADING CO., an Oregon corporation, LAWRENCE BERNARD, INDIVIDUALLY, and DR. LAWRENCE BERNARD, Professional Corporation, et al,

Respondents.

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ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

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# BRIEF FOR RESPONDENTS IN OPPOSITION

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## STATEMENT OF THE CASE

Respondents accept the Statement of the Case as set forth in the Petition with the exception of the sections pertaining to Decision of the Trial Court

and the Facts which are restated and expanded here.

1. Decision of the Trial Court

The trial judge denied Petitioner's Motion for Summary Judgment and granted Respondents' Motion for Partial Summary Judgment on the liability issue, holding that Petitioner exacted usurious interest by computing interest by the 365/360 method on loans that were at the maximum interest rates under applicable law and that such charging of usurious interest was knowingly done by Petitioner in violation of the National Bank Act.

2. Facts

Petitioner omitted the following facts material to the consideration of the questions presented:

The loan obligations entered into between Petitioner and the member borrowers of the class provided for interest at

the maximum rates under applicable law. (R 974, 975)

Petitioner computed interest by the 365/360 method on Respondents' loans and as a general practice computed interest by the 365/360 method on loans to the member borrowers of the class which were commercial loans and direct accrual installment credit loans. (R 975, 976) Such action was taken pursuant to Petitioner's Standard Practice Manual which it maintains as a guide for bank personnel and governs the operations of various banking functions. (R 975, 976)

Petitioner on occasion departs from its "normal and usual practice" of computing interest by the 365/360 method on commercial loans. (R 700)

When Petitioner computes interest by the 365/360 method the actual and precise interest rate charged is as follows:

| Indicated Rate | Actual Rate |
|---|---|
| 10% | 10.139% |
| 12% | 12.167% |

Petitioner knew that the legal rate of interest permitted to be charged on loans to individuals was 10%, and 12% on loans to corporations. (R 699)

Petitioner computes interest on regular term savings accounts on a 360/360 or 365/365 basis. (R 485)

ARGUMENT

Petitioner's contention that there is a conflict presented between the instant case and decisions of this Court, other Courts of Appeal and state law is imaginative but incorrect. There is no conflict whatsoever. The decision in this case is in complete congruence with all other cases concerning each of the questions presented in the Petition.

Neither does this case involve any matters of national significance as urged

by Petitioner and the American Bankers Association appearing as Amicus Curiae. There has never been an established uniform method of computing interest. As the Court of Appeals observed in a footnote to its opinion: "Nationwide surveys indicate that although the 365/360 method is used there is no definite, uniform, long-established custom." (Footnote No. 3, Appendix to Petitioner's Brief p 13a)

The American Bankers Association suggests that the consequences to the banking industry could be serious if the 365/360 method is prohibited. Such an exalted view of the significance of the case is unfounded. The District Court decision was rendered in 1971. As a result Petitioner and other national banks have discontinued the use of the 365/360 method. No disastrous consequences have been reported.

If they were to occur they would have surfaced by now. This case is of consequence primarily to the particular parties. The Court of Appeals considered the actual and practical effect of its decision and stated:

> " * * * We also doubt that this decision will create great hardship as the bank suggests. Our decision is limited to a construction of Oregon law. Oregon limits the usury defense to loans of less than $50,000 (if made after September, 1971). The National Bank Act contains a short two-year statute of limitations. Undoubtedly a significant number of borrowers will take advantage of this decision, but the disastrous consequences suggested by the amicus curiae, American Bankers Association, are greatly exaggerated." (Appendix to Petitioner's Brief, pp 11(a), 12(a))

It is clear that the questions involved in this case are not sufficiently important for this Court to review.

1. There is no Conflict of Decision on the Issue of "Knowingly".

Under the National Bank Act, liability for charging usurious interest is established when a national bank "knowingly" receives a greater rate of interest than allowed. 12 USC §86.

After holding that Petitioner's use of the 365/360 method in computing interest at the maximum legal rate produced a greater rate of interest than allowed by law, the District Court concluded that it was done knowingly, stating:

> "Here, it is agreed that the bank knew that its computation of interest on the 360-day year would result in the borrower paying more in one year than the maximum legal rate when computed on a calendar year. Indeed, the record shows that the bank's computers and interest charts are geared to paying the interest to depositors on the basis of a calendar year, while charging interest to Plaintiff on the basis of

> the shorter year with the resulting higher yield. Clearly, then, the bank understood full well the different financial implications between using the 360-day year in the latter case, and the 365-day year in the former." 334 F Sup 890

Petitioner, in desperation, captions its first legal argument in terms of a conflict between the instant case and other National Bank Act cases. However, an examination of Petitioner's argument and the cases cited by it discloses that there is no conflict of any kind.

Petitioner claims there was error in the lower courts' decisions because there was no evidence that it had "a specific intent to violate the usury law". The lower courts held that specific intent to violate the law was not an element of the statutory requirement of "knowingly". United States v.

International Minerals & Chemical Corporation, 402 US 558 (1970) was cited by the lower courts for the general proposition that knowledge of the facts and not knowledge of the law was sufficient to constitute a violation. While, as Petitioner points out, International Minerals was the only case cited by the Courts on the question of "knowingly", it was merely representative of many other cases discussing such issue that had been briefed, argued and considered by the courts.

Petitioner refers to an unreported District Court opinion in Cohen v. District of Columbia National Bank, (D. Columbia, 1974) which questions the applicability of International Minerals as a precedent. However, the holding in Cohen to the effect that 12 USC §86 only requires an intent to take a greater rate of

interest than allowed by law is entirely compatible with the instant case. A mere difference of opinion on the quality of authority between a District Court on the one hand, and the Court of Appeals for the Ninth Circuit, does not create a conflict warranting review by this Court.

The state court cases cited by Petitioner dealing with corrupt intent have no application in this case. In Evans v. National Bank, 251 US 108 (1919) this Court held that the National Bank Act adopted the usury law of the state where the national bank was located only insofar as determining the rate of interest. Accordingly, the meaning of the word "knowingly" is solely a question of federal law.

There can be no conflict when none of the applicable cases discussed

by Petitioner are capable of an interpretation that a specific intent to violate the law be shown. All the cases require is an intent to take payment of a greater rate of interest than that allowed by law. See, for example, First National Bank of Blakely v. Davis, 135 Ga 687, 70 SE 246 (1911) which is the leading case relied on by Petitioner and the District Judge in Cohen.

In this case, Petitioner knowingly charged excessive interest. Petitioner admits using the 365/360 method of computing interest on commercial loans. (R 975, 976) Further, Petitioner's counsel in oral argument before the District Court stated:

> "Mr. Weiner:
>
> We'll stipulate, Your Honor, that we have a manual which provides for the determination of interest by a certain way, and that our officers followed

> the manual, that they knew what the manual said and they followed it and intended to follow the manual."

Petitioner admits that in computing interest by the 365/360 method the actual and precise interest charged (10.139% and 12.167%) was in excess of the maximum lawful rates of 10% and 12% for individuals and corporations respectively. (R 700) Petitioner also knew that the maximum rates of legal interest were on loans to individuals and corporations. (R 699) Under the undisputed facts the Court of Appeals was clearly right in affirming the trial court's holding that Petitioner violated the National Bank Act. In considering this matter, the Court of Appeals stated:

> "The bank further contends that it did not intend to violate the law, so it did not knowingly exact excess interest. We disagree. While the bank may not have realized that its method of computation

> was illegal, it was agreed that the bank knew that its computation of interest on a 360-day year would result in a borrower paying more in one year than at the maximum legal rate when computed on a calendar year. The act of charging the excessive interest was intentional. This is sufficient to constitute a knowing violation of the law."

(Appendix to Petitioner's Brief, p 9a)

Petitioner contends that the Petition for Certiorari should be granted because there was no way of knowing it was violating the law. A review of the record in this case discloses otherwise.

Feldman & Hindle, The Mathematics of Business Affairs, (2d Ed 1963) is one of the text materials which Petitioner cited in answers to interrogatories to sustain its use of the 365/360 method of computing interest. The text discusses

the methods of computing interest (ordinary interest is the 365/360 basis, and exact interest is the 360/360 basis) as follows at p 22:

> "All other things being equal, lender prefers ordinary interest because he will earn a greater amount of interest; borrower prefers exact interest because he will have to pay a smaller interest charge.
>
> Lenders who normally figure ordinary interest may change to figuring exact interest when the rate is at the legal maximum (6% or 8% for most states). A rate higher than 6% would have to be used for figuring exact interest to match the amount of ordinary interest at 6%." (R 968)

4 Accountant's Encyclopedia, p 1606 (Prentice Hall 1962), another text which discusses the use of the different methods of computing interest when the rate is at the maximum, states:

> "Exact interest is usually figured by governmental agencies, by lenders whose interest rates are at the

> legal maximum, and in the case where a period of time is a larger part of a year." (Emphasis added) (R 969)

The Banking Law Journal, June, 1904, pp 423, 424 and again in the October-November 1912 issues, pp 63 and 64 states that the strict legal rule was to compute interest on the basis of 365 days to the year, and that according to some jurisdictions computing interest at the highest rate on the basis of 360 days to the year amounts to usury.

From the cases involving the use of the 365/360 method of computing interest Petitioner could have learned that the illegality of such method had been established in some jurisdictions. In The New York Firemen Insurance Company v. Ely and Parsons 2 COW 678 (NY 1824), the first case to consider the calculation of interest by the 365/360 method, the Court concluded that it was usurious to use such method

when the interest rate was as the maximum.

The Bank of Utica v. Wager, 2 COW 712 (NY 1824) aff'd 8 COW 398 (1826) likewise held that it was usurious to compute interest by the 365/360 method. The Court stated at p 762:

> " * * * There is nothing to take it out of the operation of the principle established in The Firemen Insurance Co. v. Ely and Parsons; that this mode of calculating the interest renders the transaction usurious."

The same rule was followed in Utica Insurance Company v. Tilman, 1 Wend 555 (NY 1826), Bank of Utica v. Smalley & Bernard, 2 COW 770 (NY 1824) Aff'd 8 COW 398 (1826) and Hass v. Flint, 8 Blackf 67 (Ind 1846).

Silverstein v. Shadow Lawn Savings and Loan Association, 51 NJ 30, 237 A2d 474 (1968), the latest case dealing with this subject matter, held that it was a breach of contract to use the 365/360 method of computing interest. Dowler v. Georgia Enterprises, Inc., 162 Tenn 59,

34 SW 2d 445 (1931) held that it was wrong to compute interest by 360 instead of 365 days in a year. Ditmars v. Camden Trust Co., 10 NJ 471, 92 A2d 12 (1952), one of the most recent cases, held it was illegal to calculate interest by the 365/360 method at the maximum statutory rate.

In this case Petitioner disregarded the case law and the text authorities and opted in favor of obtaining a greater amount of interest which of course was one of the chief purposes of the use of the 365/360 method as recognized by its innovator, Mr. Rowlett. (Brief of Amicus Curiae American Bankers' Association, p 14). Such action of Petitioner in receiving a greater rate of interest was done "knowingly" and constitutes a violation of the National Bank Act.

Under any view of the decisions there is no real conflict in the cases as to the requisite intent to establish

a violation of the National Bank Act. The decisions of the lower courts were clearly correct. This issue does not require review by this Court on certiorari.

2. The Court Correctly applied Federal Law and Correctly Decided that Respondent was Entitled to Partial Summary Judgment.

On the question of custom Petitioner asserts the dual argument that under applicable federal law custom was not taken into account, and secondly that the court erred in ruling on the Motions for Summary Judgment since the facts as to an alleged custom of computing interest were disputed. Neither issue warrants review by this Court on certiorari.

All of the applicable law to include what Petitioner refers to as the "landmark case" of Evans v. National Bank, discussed supra, was recognized and

followed by the lower courts. (See Court of Appeals Opinion p 7a, Appendix Petitioner's Brief.) The District Court did not rule that custom could not be considered. As a matter of law the District Court rejected Petitioner's contention that there was a custom to sustain the use of the 365/360 method of computation to obtain interest in excess of the legal rate. By way of explanation the District Court commented that it was doubtful that the practice could ever be legitimized because only in periods of heavy borrowing and high interest would the question arise. In other words, the critical inquiry is not whether the 365/360 method is used generally, but whether there is an established use of such method when the interest rates are at the legal maximum to sanction receipt of the excess interest.

Petitioner's brief does not mention that Petitioner filed a Motion for Summary

Judgment in this cause "upon the ground that there is no genuine issue of material fact". (R 582) Curiously, Petitioner now argues that the facts as to custom were "hotly disputed". In support of its claimed custom, Petitioner points out that it relied upon certain cases, Answers to Interrogatories that referred to textbooks describing the practice, and a study by Congressman Wright Patman. The main thrust of the argument by the American Bankers Association which joins Petitioner in this cause as amicus curiae is that the lower courts did not recognize the "ancient custom" of computing interest by the 365/360 basis. A review of the record shows that there is no genuine issue of fact on the question of custom.

The Court of Appeals commented in footnote No. 3 of its opinion on the study by Congressman Patman which purportedly reflects the custom:

> "Nationwide surveys indicate that although the 365/360 method is used, there is no definite, uniform, long-established custom. The results of a Federal Reserve Board survey were summarized by Congressman Patman as follows:
>
> 'This practice [use of the 365/360 method] is not standard or uniform in any way. It varies among banks with respect to the types of loans or maturities of loans subjected to the practice. It varies even in many instances within the same bank with respect to the type of loans and maturity of loans to which the practice is applied, and it varies significantly from one part of the country to another. 117 CONG REC 18539 (1971) (Remarks of Congressman Patman)'"

In some of the cases cited by Petitioner the use of the 365/360 method of computing interest was permitted when consistent with a long-established custom on the ground that it negated the requirement of a corrupt agreement. However, most of the cases were decided over one hundred years ago, so that the practice prevailing then would not be relevant today.

Of the textbooks listed by Petitioner in its Answers to Interrogatories, only one, Feldman & Hindle, The Mathematics of Business Affairs, supra, discusses the practice of using the 365/360 method at the maximum interest rates, and such authority is contrary to Petitioner's claim of custom. Such text and 4 Accountants' Encyclopedia, supra, both state that normally and usually lenders do not compute interest by the 365/360 method when the rates are at the legal maximum.

The record further shows that as to savings and loan associations, government agencies and other institutions there is no custom regarding the use of the 365/360 method of computing interest.

A survey made by the Federal Home Loan Bank Board indicated that of 871 institutions responding to the survey, 802 used the 360/360 method of computing interest, and 51 used the 365/365 method.

Only 18 of the institutions surveyed, all located in the Little Rock Bank District, used the 365/360 method. (R 965, 967)

For over 50 years interest on loans which Petitioner obtained from the Federal Reserve Bank has been computed on the 365/365 basis. (R 703)

The Department of Veterans' Affairs and the Division of Lands of the State of Oregon compute interest on their loans on a 360/360 basis. (R 703)

The Oregon State Accident Insurance Fund computes interest on its loans on a 360/360 basis. (R 704)

As for Petitioner's own practice, the record discloses no consistent use of the 365/360 method of computing interest. Petitioner does not compute interest on all loans on the 365/360 basis, but uses the 360/360 basis for real estate loans, direct mobile home loans, and on installment credit loans. (R 976)

Even within the commercial loan classification Petitioner does not consistently charge on a 365/360 basis. (R 700) Petitioner in paying its depositors interest on savings accounts computes interest on a 360/360 or 365/365 basis. (R 485) So insofar as Petitioner's own practice, it borrows money on a 365/365 basis, pays interest to most of its depositors on a 365/365 or 360/360 basis, charges interest on some classes of loans on a 365/365 or 360/360 basis, and on other classes on a 365/360 basis, and only charges some customers of its commercial loan department interest on a 365/360 basis, charging others on a 365/365 or a 360/360 basis.

The lower courts were correct in holding that no custom exists sufficient to exculpate Petitioner from charging usurious interest.

3. There is no Direct Conflict Between Courts of Appeal on the Small Loan Issue.

Petitioner argues that there has been no violation of the National Bank Act in this case, since it can charge 36% on its loans, which is the rate small loan companies charge in the State of Oregon. In support of such position and the further contention that there is a conflict between Courts of Appeal, Petitioner cites Northway Lanes v. Hackley Union National Bank & Trust Co., 464 F2d 855 (CA 6 1972). There is no actual conflict in the decisions because Northway Lanes deals with savings and loan association charges and does not involve an attempt to charge a rate applicable to a small loan company.

Under the National Bank Act, Petitioner can charge interest at the general rate of interest, or the rate allowed

state banks, whichever is greater. 12 USC §85. The general rate of interest in Oregon is 10% and 12% for individuals and corporations respectively. ORS 82.010. State banks in Oregon cannot charge interest at the small loan company rate of 36%. ORS 707.310(6). The lower courts were correct in holding that Petitioner charged usurious interest by exceeding the rates of 10% and 12%.

4. There is no Conflict with State Law Respecting the Non-Retroactive Application of Oregon Legislation Removing the Defense of Usury.

Petitioner contends that a 1971 Oregon statute which removes the defense of usury on loans of $50,000.00 or more enacted after this cause was filed with the District Court applies retroactively to bar this claim for charging usurious interest. A review and determination by the U. S. Supreme Court is not necessary because such issue

involves an esoteric matter of state law which was correctly decided by the Ninth Circuit Court of Appeals and which does not conflict with any state court decision.

The penalty for charging usurious interest is conferred by federal law. 12 USC § 86. ORS 82.125 simply removed the defense of usury on transactions of $50,000 or more. Petitioner argues that "Where a statute repeals a penalty, the repealing statute is given retroactive application". The penalty provided in the National Bank Act was not repealed by an Oregon State statute.

The Oregon law is well settled and as stated by the Ninth Circuit Court of Appeals:

> "Absent a clear, express intention, legislation in Oregon is not normally applied retroactively. Seton v. Hoyt, 34 Or 266, 55 P 967 (1899); Smith v. Clackamas County, 252 Or 230, 448 P2d 512 (1968). Nothing in either the language of the statute or the legislative history indicate a desire to

eliminate causes of action that had already accrued prior to the passage of the act." (Opinion pp 10a and 11a, Appendix, Petitioner's Brief)

## CONCLUSION

For the foregoing reasons it is respectfully submitted that the Petition for a Writ of Certiorari be denied.

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